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MONTANA LOTTERY

FINANCIAL STATEMENTS (Unaudited)

March 31, 2003

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(Unaudited)

March 31, 2003

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APPOINTIVE OFFICIALS

Gerald J. LaChere, Lottery Director

L. John Onstad, Lottery Assistant Director for Security

LOTTERY COMMISSION

TERM EXPIRES

Clifford Brophy	Columbus	January 1, 2005
Donald Sterhan	Billings	January 1, 2005
Tom Keegan	Helena	January 1, 2006
Betty Wilkins	Missoula	January 1, 2006
Robert Crippen	Butte	January 1, 2007

REPORT DISTRIBUTION

According to Section 23-7-202(9), MCA, copies of this report must be distributed to the following:

Governor - Judy Martz
Director of Dept. of Administration – Scott Darkenwald
Legislative Auditor - Scott Seacat
President of the Senate – Bob Keenan
Speaker of the House – Doug Mood

The law also states "the President of the Senate and the Speaker of the House will determine the report distribution to each member of the appropriate committee of each house of the legislature".

The President of the Senate and the Speaker of the House have requested that this report be distributed to the following committees:

HOUSE – State Administration Committee

Debby Barrett, Chair	Ralph Lenhart
Dee Brown, Vice Chair Majority	Alan Olson
Larry Jent, Vice Chair Minority	Bernie Olson
Norman Ballantyne	Don Roberts
Arlene Becker	Clarice Schrupf
Sue Dickenson	Frank Smith
Carol Gibson	Pat Wagman
Dan Hurwitz	Jonathan Windy Boy
Hal Jacobson	Cindy Younkin
Larry Lehman	

HOUSE – Business & Labor Committee

Joe McKenney, Chair	Ray Hawk
Don Steinbeisser, Vice Chair Majority	Bob Lawson
Jim Keane, Vice Chair Minority	Rick Maedje
Bob Bergren	Gary Matthews
Rod Bitney	Scott Mendenhall
Sylvia Bookout-Reinicke	Penny Morgan
Nancy Rice Fritz	Allen Rome
Dave Gallik	Sandy Weiss
Kathleen Galvin-Halcro	Bill Wilson

SENATE – State Administration Committee

John Cobb, Chair	Carolyn Squires
Mike Sprague, Vice Chair	Mike Wheat
Kelly Gebhardt	

SENATE – Business & Labor Committee

Dale Mahlum, Chair	Sam Kitzenberg
Mike Sprague, Vice Chair	Ken Hansen
Sherm Anderson	Glenn Roush
Vicki Cocchiarella	Don Ryan
Kelly Gebhardt	Carolyn Squires
Bob Keenan	Fred Thomas

Montana Lottery

June 2003

Montana Lottery Commission:

The close of fiscal year 2003 marks the end of another successful year for the Lottery. Revenues totaled \$34,696,380, approximately \$1 million greater than fiscal year 2002 and very close to our budget goal. The General Fund transfer of \$7,453,281 exceeded our projected goal by \$613,282.

Sales results vary by product. Scratch ticket sales exceeded last year by \$360.634 based upon strong sales for *Slingo*. The other scratch ticket price points sales remained steady. Hot Lotto is proving to be much more popular than Rolldown with almost double the annual sales. Powerball sales increased slightly but both Wild Card and Montana Cash did have decreases from the previous year.

Direct game costs increased by \$697,301 as a result of high game sales. This increase was less than the usual proportionate amount of sales because of an unclaimed Powerball jackpot; the Lottery received a refund of \$333,626 in March for its portion.

The Lottery held operating expenses to about the same level as last year, with an overall increase of only \$38,010. Expense categories with an increase were depreciation and employee salaries, while public relations and premium expense had decreases.

In conclusion, we believe that with General Fund Transfers exceeding \$7.4 million for the past two years that the Lottery has moved up to a transfer level that will remain in the \$7 million range from the transfer level of \$6 million which was achieved in fiscal years 1997 through 2001.

Sincerely,



Gerald J. LaChere
Director



MONTANA LOTTERY
STATEMENT OF NET ASSETS
JUNE 30, 2003 and 2002
(UNAUDITED)

	Period Ended June 30, 2003	Period Ended June 30, 2002
ASSETS:		
CURRENT ASSETS		
Cash and Cash Equivalents	\$ 244,733	\$ 391,199
Receivables (Net)	1,248,689	796,271
Due from Other Funds	584	2,646
Inventories	607,261	812,944
Other Current Assets	<u>30,970</u>	<u>12,505</u>
TOTAL CURRENT ASSETS	2,132,237	2,015,565
NONCURRENT ASSETS		
Computer, Furniture & Equipment	5,589,216	5,562,699
Accumulated Depreciation	(3,086,306)	(2,208,177)
Software, net of Amortization	451,785	616,071
Other Intangibles	0	6,582
Multi-State Receivable	<u>1,742,643</u>	<u>2,100,876</u>
TOTAL NONCURRENT ASSETS	4,697,338	6,078,051
TOTAL ASSETS	\$ <u>6,829,575</u>	\$ <u>8,093,616</u>
LIABILITIES:		
CURRENT LIABILITIES		
Accounts Payable	\$ 475,299	\$ 1,035,859
Estimated Prize Liability	1,340,477	1,336,547
Due to Other Funds	35,013	10,449
Transfer Obligations	1,811,272	1,591,454
Deferred Revenue	173,133	78,821
Current Portion Comp. Absences	107,343	101,424
Current Portion Long-Term Debt	<u>1,109,836</u>	<u>1,054,786</u>
TOTAL CURRENT LIABILITIES	5,052,373	5,209,340
NONCURRENT LIABILITIES		
MUSL Prize Liability	1,699,206	1,707,049
Note Payable	0	1,109,836
Accrued Compensated Absences	<u>77,996</u>	<u>67,391</u>
TOTAL NONCURRENT LIABILITIES	1,777,202	2,884,276
TOTAL LIABILITIES	6,829,575	8,093,616
NET ASSETS		
Unrestricted Net Assets	<u>0</u>	<u>0</u>
TOTAL LIABILITIES AND NET ASSETS	\$ <u>6,829,575</u>	\$ <u>8,093,616</u>

The accompanying notes are an integral part of these financial statements

MONTANA LOTTERY
STATEMENT OF REVENUES, EXPENSES AND CHANGES IN FUND NET ASSETS
FOR THE QUARTERS ENDED JUNE 30, 2003 and 2002
(Unaudited)

	Quarter Ended June 30, 2003	Quarter Ended June 30, 2002	Twelve Months Ended June 30, 2003	Twelve Months Ended June 30, 2002
OPERATING REVENUES:				
Instant ticket revenue	\$ 2,565,286	\$ 2,478,998	\$ 10,134,734	\$ 9,774,100
Powerball revenue	3,683,376	3,197,041	15,979,707	15,715,054
Montana Cash revenue	1,216,791	997,083	3,961,639	4,416,477
Wild Card revenue	545,208	593,241	2,387,858	2,597,262
Hot Lotto/Rolldown revenue	528,723	632,148	2,218,556	1,129,380
900 # Income	(84)	6,455	8,980	36,166
License, permits, and misc	1,062	300	4,906	1,885
Total Operating Revenues	8,540,362	7,905,266	34,696,380	33,670,324
Less Direct Game Costs:				
Instant ticket prize expense	(1,464,543)	(1,431,245)	(5,918,176)	(5,643,263)
On-line ticket prize expense	(2,764,696)	(2,680,992)	(11,644,782)	(11,460,703)
Retailer commission	(496,028)	(470,070)	(2,035,751)	(1,982,254)
Cost of tickets sold	(211,614)	(171,377)	(759,549)	(665,735)
Vendor fees	(703,597)	(653,672)	(2,899,115)	(2,808,117)
Total Direct Game Costs	(5,640,478)	(5,407,356)	(23,257,373)	(22,560,072)
Income Before Operating Expenses	2,899,884	2,497,910	11,439,007	11,110,252
OPERATING EXPENSES:				
Advertising	152,350	210,682	555,402	566,253
Advertising Production	76,669	57,179	158,736	183,510
Audit Fees	35,303	3,541	58,264	27,793
Bad Debts Expense	1,021	(90)	908	(292)
Communications	20,326	23,457	83,602	99,067
Contractual Services	56,223	37,600	145,505	149,839
Depreciation and Amortization	265,324	230,753	1,053,362	870,071
Interest Expense	15,554	29,303	81,041	133,844
Management Service Fee	11,815	17,722	70,888	70,888
Multi-State Dues	0	0	89,435	76,426
Public Relations	3,692	7,693	25,784	61,849
Other	9,671	10,834	35,542	37,363
Personal Services	345,528	318,757	1,382,005	1,260,507
Repairs and Maintenance	10,473	7,165	27,324	22,226
Supplies and Materials	67,037	171,086	160,915	336,859
Travel	7,829	9,122	27,250	28,418
Utilities and Rent	27,523	27,454	106,443	99,775
Total Operating Expense	1,106,338	1,162,258	4,062,406	4,024,396
Operating Income	1,793,546	1,335,652	7,376,601	7,085,856
NONOPERATING REVENUES (EXPENSES)				
Interest earnings	17,726	20,227	77,140	145,599
Security Lending Income	0	825	0	825
Security Lending Expense	0	(739)	0	(739)
Gain/Loss on sale of asset	0	(2,194)	(460)	(2,194)
Total Nonoperating Revenues(Expenses)	17,726	18,119	76,680	143,491
Income Before Operating Transfers	1,811,272	1,353,771	7,453,281	7,229,347
Operating Transfers In (Out) - General Fund	(1,811,272)	(1,591,454)	(7,453,281)	(7,467,030)
CHANGE IN NET ASSETS	0	(237,683)	0	(237,683)
Total Net Assets, Beginning of Period	0	237,683	0	237,683
TOTAL NET ASSETS, END OF PERIOD	0	0	0	0

The accompanying notes are an integral part of these financial statements.

MONTANA LOTTERY
STATEMENT OF REVENUES, EXPENDITURES AND CHANGES IN NET FUND ASSETS
AND RECONCILIATION OF BUDGET AND ACTUAL (BUDGETARY BASIS) TO GAAP BASIS
FOR THE TWELVE MONTHS ENDED JUNE 30, 2003
(Unaudited)

	<u>Budget</u> Fiscal Year July 1, 2002 - June 30, 2003	<u>Actual</u> Fiscal Year Ended June 30, 2003 (Unaudited)	Actual as a Percent of Final Budget (%)
REVENUES:			
Instant ticket revenue	\$ 10,200,000	\$ 10,134,734	99.36
Powerball revenue	15,200,000	15,979,707	105.13
Montana Cash revenue	4,100,000	3,961,639	96.63
Wild Card revenue	2,600,000	2,387,858	91.84
Hot Lotto revenue	2,900,000	2,218,556	76.50
900 # Income	25,000	8,980	35.92
License, permits, and miscellaneous	2,000	4,906	245.30
Total Revenues	<u>35,027,000</u>	<u>34,696,380</u>	99.06
DIRECT GAME COSTS			
Prizes - instant ticket	5,916,000	5,918,176	100.04
Prizes - on-line games	12,295,000	11,644,782	94.71
Retailer commissions	2,056,000	2,035,751	99.02
Ticket cost - instant games	728,000	759,549	104.33
Ticket cost - vendor fees	2,922,500	2,899,115	99.20
Total Direct Game Costs	<u>23,917,500</u>	<u>23,257,373</u>	97.24
OPERATING EXPENSES:			
Advertising	637,576	555,402	87.11
Advertising Production	147,200	158,736	107.84
Audit Fees	60,000	58,264	97.11
Communications	100,015	83,602	83.59
Contractual Services	250,011	145,505	58.20
Interest Expense	81,041	81,041	100.00
Management Service Fee	75,000	70,888	94.52
Multi-State Dues	114,881	89,435	77.85
Public Relations	75,950	25,784	33.95
Other	46,569	35,542	76.32
Personal Services	1,353,906	1,365,481	100.85
Repairs and Maintenance	27,052	27,324	101.01
Supplies and Materials	200,775	160,915	80.15
Travel	40,490	27,250	67.30
Utilities and Rent	108,288	106,443	98.30
Equipment	21,627	39,396	182.16
Total Operating Expenses	<u>3,340,381</u>	<u>3,031,008</u>	90.74
Operating Income	7,769,119	8,407,999	108.22
NONOPERATING REVENUES (EXPENSES):			
Interest Earnings	0	12,508	
Security Lending Transactions		0	
Loss on Sale on Asset		(460)	
NET INCOME (BUDGETARY BASIS)	<u>\$ 7,769,119</u>	<u>\$ 8,420,047</u>	108.38
RECONCILIATION OF BUDGETARY/GAAP BASIS:			
1 Capitalized equipment purchases	21,627	39,396	182.16
2. Adjustment for compensated absences		(16,524)	
3. Adjustment for depreciation expense	(1,070,747)	(1,053,362)	98.38
4 Bad Debts		(908)	
5 MUSL interest earnings	<u>120,000</u>	<u>64,632</u>	53.86
Total Reconciling Items	(929,120)	(966,766)	
NET INCOME (GAAP BASIS)	<u>\$ 6,839,999</u>	<u>\$ 7,453,281</u>	108.97

The accompanying notes are an integral part of these financial statements.

MONTANA LOTTERY
ANALYSIS OF REVENUES AND EXPENSES BY PRODUCT
FOR THE TWELVE MONTHS ENDED JUNE 30, 2003
(UNAUDITED)

	INSTANT	POWERBALL	MONTANA CASH	WILD CARD	HOT LOTTO	ADMIN
REVENUES:	\$ 10,134,734	\$ 15,979,707	\$ 3,961,639	\$ 2,387,858	\$ 2,218,556	\$ 13,886
DIRECT GAME COSTS						
Prize Expense	5,918,176	7,299,334	1,976,495	1,249,600	1,119,353	0
Retailer Commissions	807,717	799,510	198,127	119,435	110,962	0
Cost of Tickets Sold	759,549	0	0	0	0	0
Vendor Fees	811,752	1,358,798	336,869	203,046	188,650	0
INCOME BEFORE OPERATING EXPENSES	1,837,540	6,522,065	1,450,148	815,777	799,591	13,886
OPERATING EXPENSES:						
Advertising	198,817	211,247	48,822	48,097	47,729	690
Advertising Production	34,050	39,868	28,273	28,273	28,272	0
Audit Fees	0	0	0	0	0	58,264
Bad Debts	0	0	0	0	0	908
Communications	45,887	210	210	210	210	36,875
Contractual Services	24,859	2,910	2,910	2,910	2,910	109,007
Depreciation and Amortization	296,853	489,656	121,860	73,370	68,212	3,411
Interest	22,692	37,983	9,417	5,676	5,273	0
Management Service Fee	27,095	8,408	5,814	4,301	4,044	21,226
Multi-State Dues	0	12,419	0	39,369	13,348	24,299
Public Relations	8,119	3,258	3,258	3,258	3,258	4,633
Other	670	44	44	44	44	34,696
Personal Services	484,361	170,185	120,613	82,535	79,986	444,325
Repairs and Maintenance	205	51	51	51	51	26,914
Supplies and Materials	52,911	5,766	5,438	5,357	5,357	86,086
Travel	3,070	768	768	768	768	21,108
Utilities and Rent	0	0	0	0	0	106,443
TOTAL OPERATING EXPENSES	1,199,589	982,773	347,478	294,219	259,462	978,885
OPERATING INCOME	637,951	5,539,292	1,102,670	521,558	540,129	(964,999)
NONOPERATING REVENUES (EXPENSES)						
Security Lending Transactions	0	0	0	0	0	0
Interest Earnings	0	0	0	0	0	77,140
Gain(Loss) on Sale of Asset						(460)
TOTAL NONOPERATING REVENUES (EXPENSES)	0	0	0	0	0	76,680
NET INCOME BY PRODUCT	\$ 637,951	\$ 5,539,292	\$ 1,102,670	\$ 521,558	\$ 540,129	\$ (888,319)
PROFIT AS A % OF REVENUE	6.29%	34.66%	27.83%	21.84%	24.35%	N/A

NOTE: THIS IS ONLY ONE YEAR'S ACTIVITY AND THEREFORE SHOULD NOT BE INTERPRETED TO SHOW HOW OUR PRODUCTS HAVE PERFORMED IN PAST YEARS OR WILL PERFORM IN THE FUTURE.

MONTANA LOTTERY
Notes to the Financial Statements (Unaudited)
March 31, 2003

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Reporting Entity.

The Montana Lottery, established under the provisions of Section 23-7-101, Montana Code Annotated (MCA), was approved by the Montana electorate through Legislative Referendum No. 100 on November 4, 1986.

Montana's first lottery tickets went on sale June 24, 1987.

The Montana Lottery is operated by a five-member commission consisting of Montana residents appointed by the Governor. The Commission, by law, has the power to operate a state lottery, determine the types and forms of lottery games, set the ticket price, number and size of prizes, conduct lottery drawings, enter into agreements to offer lottery games in conjunction with other lottery states and prepare financial reports. The Montana Lottery is attached to the Montana Department of Administration for administrative purposes.

The Montana Lottery is included as an enterprise fund in the State of Montana's Comprehensive Annual Financial Report. In accordance with governmental accounting and financial reporting standards, there are no component units to be included within the Montana Lottery's financial statements as a reporting agency.

Basis of Presentation. The Montana Lottery reports its financial activity in accordance with generally accepted accounting principles (GAAP) as prescribed in pronouncements of the Governmental Accounting Standards Board (GASB).

Enterprise Fund. The Montana Lottery is classified as an Enterprise Fund of the Governmental Proprietary Fund Type. Enterprise Funds account for operations: a) financed and operated similar to private business enterprises, where the intent of the Legislature is that costs are to be financed or recovered primarily through user charges, or b) where the Legislature has decided that periodic determination of revenue earned, expenses incurred, or net income is appropriate.

Basis of Accounting. The Montana Lottery's financial statements are prepared using the accrual basis of accounting. Revenues are recognized in the accounting period in which they are earned and become measurable; expenses are recognized in the period incurred, if measurable.

Revenue Recognition. Lottery instant ticket sales are recorded as revenue based on the time the retailer activates the pack of tickets for sale. In accordance with an established policy, retailers may return unsold tickets to the Lottery for credit. Sales are decreased by an allowance for estimated ticket returns.

Lottery on-line ticket sales are recorded as revenue based on drawings. Tickets sold in advance for future drawings are recorded as deferred revenue until such time as the tickets become valid for the most current drawing.

Free Tickets. Some Montana Lottery instant games award free tickets as prizes. Net lottery ticket revenue does not include the value of free tickets given away and free plays won. The face value of these free ticket prizes distributed for the quarter and nine months ended March 31, 2003 was \$148,524 and \$284,442 respectively.

Promotional Credits. The Lottery issues promotional credits to retailers to be used to distribute free tickets to players. The tickets are distributed as part of a promotion run by the retailer, e.g., "Ask for the Sale" or second chance drawings. The lottery also directly distributes instant tickets for promotional purposes at trade shows, for media give-aways, and during new game introductions. The tickets distributed as a result of promotional credits are reflected as a reduction in revenue. The related prize expense and ticket cost for all promotions are reclassified as an advertising expense. For the quarter ended March 31, 2003, promotional credits resulted in a revenue reduction of approximately \$11,495 and an advertising expense reclassification of approximately \$9,726. For the nine months ended March 31, 2003, promotional credits resulted in a revenue reduction of approximately \$53,753 and a prize expense reclassification of approximately \$41,638.

Prizes. Expenses for instant prizes are recorded based on the predetermined prize structure for each game. Expenses for on-line prizes are recorded based on the predetermined prize structure for each on-line game. No prize expense is recorded for free tickets distributed.

Unclaimed Prizes. Prizes for the online games, Powerball, Wild Card, Montana Cash, and Hot Lotto, must be claimed within six months after the appropriate draw date. Prizes for instant games must be claimed within six months of the announced end of each game. The unclaimed prize amounts are taken as a reduction in the Lottery Prizes Payable liability and the Prize Expense and are transferred to the State of Montana General Fund as a portion of the quarterly transfer. The amount of unclaimed prizes for all games is represented in the table below.

	Quarter Ended 3/31/03	Quarter Ended 3/31/02	Year To Date 3/31/03	Year To Date 3/31/02
Online	\$512,923	\$224,023	\$724,304	\$668,859
Instant	<u>146,044</u>	<u>81,035</u>	<u>220,246</u>	<u>253,725</u>
TOTALS	\$658,967	\$305,058	\$944,550	\$922,584

2. SUMMARY OF ACCOUNTS

Cash and Cash Equivalents. Cash and cash equivalents consist of interest-bearing deposits with the Montana Board of Investments short-term investment pool, cash on deposit with a bank and cash on deposit with the Montana State Treasurer that is part of the State's pooled cash and is not separately identifiable as to specific types of securities. These funds are highly liquid and may be drawn on daily.

Cash and cash equivalents consist of the following:

	March 31,	
	<u>2003</u>	<u>2002</u>
Short-term investment pool	\$250,255	\$489,857
Cash on deposit with State Treasurer	131,592	373,854
Cash in revolving deposit account	10,000	10,000
Petty Cash	150	150
TOTALS	<u>\$391,997</u>	<u>\$873,861</u>

Reference to the State of Montana's Comprehensive Annual Financial Report would identify the level of risk associated with cash and cash equivalents in the short-term investment pool and amounts retained with the State Treasurer. The bank balance of the revolving deposit account was \$12,233 at March 31, 2003 and was covered by federal depository insurance. The carrying amount reported in the balance sheet for cash and cash equivalents approximates the fair market value.

Receivables. Receivables include \$1,319,539, representing amounts due the Lottery for tickets purchased by retailers. An allowance for doubtful accounts is reported as net of receivables and is based on historical perspective. As of March 31, 2003 the allowance is zero. An allowance for ticket returns is also included in the receivables amount. This allowance represents a reduction in receivables at March 31, 2003, for estimated ticket returns. This is an estimate based on returns received to date, as well as, an estimate of tickets unsold by retailers for games that

have a public sale end date prior to April 1, 2003. The allowance for ticket returns is \$196,325 at March 31, 2003. The return of vendor fees related to the allowance for returns is \$16,393.

Inventories. Inventories consist of merchandise and supplies inventories. Merchandise inventory includes lottery tickets valued at \$751,962 stored in the warehouse, at retailers prior to being activated by the retailer and with the marketing representatives. These ticket inventories are recorded at cost using the specific identification method and maintained on a perpetual inventory system. Tickets are charged to cost of tickets sold upon activation or after game end.

Supplies inventories include ticket dispensers, premiums and point-of-sale materials. At quarter end, supplies inventories totaled \$82,467. These inventories are also recorded at cost using the specific identification method.

Other Current Assets. Other current assets consist of the following:

	March 31,	
	<u>2003</u>	<u>2002</u>
Prepaid Expenses	6,284	3,216
Employee Advances	<u>5,682</u>	<u>4,800</u>
TOTALS	\$11,966	\$8,016

Transfer Obligations. The account "Transfer Obligations" is \$1,906,423 payable to the General Fund at March 31, 2003.

Compensated Absences. State employees earn vacation leave ranging from 15 to 24 days per year depending on the individual's years of service. Vacation leave may be accumulated not to exceed two times the maximum number of days earned annually. With no limit on accumulation, sick leave is earned at 12 days per year. Upon retirement or termination, an employee is paid 100% for unused vacation and 25% for unused sick leave. The Lottery's liability for compensated absences is detailed below.

Balance	Net Leave	Balance
<u>June 30, 2002</u>	<u>Earned/(Used)</u>	<u>March 31, 2003</u>
\$168,815	\$13,570	\$182,385

Commissions. Section 23-7-301(10), MCA, provides retailers a commission on instant and on-line tickets or chances sold. The Lottery Commission established this commission at 5% of the face value of instant tickets activated by the retailers and the face value of tickets sold for each on-line drawing. For the quarter and the nine months ended March 31, 2003 commissions totaled \$467,996 and \$1,539,723 respectively.

Included in this amount are retailers' bonus commissions on tickets sold based on incremental sales of instant tickets. During the quarter and nine months ended March 31, 2003 retailers earned bonus commissions of \$70,069 and \$226,649 respectively.

3. MARKETING PRODUCTION EXPENSES

The Lottery has contracted with several vendors to provide marketing related services and materials. These services include media placement, creative design and layout, and media production. Those services and materials not included in the Advertising and Advertising Production expense categories are printing and ticket dispensers. The cost of these services and materials, included in Operating Expenses as Contracted Services and Supplies and Materials, are detailed below for the quarter ended March 31, 2003:

Printing	\$34,712
Ticket Dispensers	<u>12,213</u>
	\$46,925

4. PAYMENTS TO OTHER STATE AGENCIES

The Lottery receives a variety of services and supplies and materials from other state agencies. These services and materials are detailed below for the quarter ended March 31, 2003:

Insurance	\$ 7,064
Warrant Writing Services	407
Payroll Services	684
Audit Fees	7,202
Work Study Contracts	6,483
Computer Fees	18,977
Printing	2,433
State Accounting System Support	10,625
Supplies and Materials	5,761
Mail Processing Fees	4,974
Telecommunications	17,611
Public Relations	7,000
Indirect Costs	65,385
Other	<u>2,388</u>
TOTAL	\$156,994

5. PRIZES

Paid Prizes. Section 23-7-402, MCA states, "A minimum of 45% of the money paid for tickets or chances must be paid as prize money". Prize expense is recorded based on the predetermined prize structure percentage for each game. For the quarter ended March 31, 2003, the prize expense of \$3,751,884 is 47.51% of net Lottery ticket revenue of \$7,897,092. For the nine months ended March 31, 2003, the prize expense of \$13,333,719 is 51.00% of net Lottery ticket revenue of \$26,143,110.

6. TRANSFER TO STATE GENERAL FUND

Section 23-7-402(3), MCA, states "That part of all gross revenue not used for payment of prizes, commissions, and operating expenses, together with the interest earned on the gross revenue while the gross revenue is in the enterprise fund, is net revenue. Net revenue must be transferred quarterly from the enterprise fund established by 23-7-401 to the State General Fund." For the quarter ended March 31, 2003, the net revenue payable to the State General Fund totaled \$1,906,423.

7. MULTI-STATE LOTTERY JOINT VENTURE

In November 1989 the Montana State Lottery joined the Multi-State Lottery Association (MUSL). MUSL was created in September 1987 to operate a multi-state lottery game for the benefit of party lotteries. Powerball, Wild Card, and Hot Lotto are the games jointly operated by the members, in which Montana presently participates. Each lottery participating in MUSL is represented on the Board of Directors.

The Multi-State Lottery Receivable with a balance of \$1,728,215, as of March 31, 2003 is comprised of several reserve accounts, which are maintained by the Multi-State Lottery Association (MUSL). The balance of these reserve accounts is as follows:

Powerball Prize Reserve Account	\$791,538
Powerball Unreserved Account	28,408
Powerball Set Prize Reserve Account	506,421
Wild Card Reserve Account	401,848
Hot Lotto Set Prize Reserve Account	0
TOTAL	\$1,728,215

The Powerball Prize Reserve Account is to be used only in the event of an unanticipated prize claim. It is an insurance fund intended to protect the member lotteries against the liability that could result from a system failure at one of the member lotteries. All money paid to this fund would be returned to the Lottery one year after the Lottery leaves the Powerball game, assuming that no unanticipated prize claims have been paid. Interest earned on the Lottery's share of the fund, represented by the Unreserved Account, would be returned to the Lottery upon leaving MUSL. The amounts in the Unreserved Account may be used at the Board's discretion.

The Powerball Set Prize Reserve Account is used to fund prize payments for current drawings. Since the Powerball game has fixed prizes, it is often necessary to draw from this reserve to fund payment of prizes at the fixed amount. This account would be returned to the Lottery upon withdrawal from the Powerball Game.

The Lottery contributes to these reserve funds through the 50% set aside for prizes. In addition the Lottery was required to contribute for its portion of the reserve funds accumulated since the start of the Powerball game. The Lottery made this payment in full as of June 1990, through an additional 2% of drawing revenue rather than making a lump sum payment. Payments made to this fund are considered a portion of prize expense associated with the game.

The Wild Card Reserve Account is to be used in the event of an unanticipated prize claim on the Wild Card game. This account is also administered by MUSL and would be returned to the Lottery one year after the Wild Card Product Group of Idaho, Montana and South Dakota is disbanded. The Lottery contributes to this account through the 55% set aside for prizes. Payments made to this fund are considered a portion of prize expense related to the Wild Card game.

The Hot Lotto Set Prize Reserve Account is administered by MUSL and is to be used only in the event of unanticipated prize claims. Hot Lotto replaced the Rolldown game on April 7, 2002, and the amount in the Rolldown Set Prize Reserve Account was transferred to the Hot Lotto reserve account. Like other MUSL games the reserve amount would be returned to the Lottery one year after withdrawal from the Hot Lotto game. The Lottery contributes to the reserve through the 50% set aside for prizes. Payments made to the reserve are considered a portion of the prize expense related to the game.

8. GAMES

Currently, the Montana Lottery games are instant ticket games and four on-line games referred to as Powerball, Montana Ca\$h, Wild Card, and Hot Lotto.

Instant ticket games provide players the opportunity to win instantly by scratching a latex covering to reveal a prize.

The Powerball game allows players the chance to win a minimum pari-mutuel jackpot of approximately \$10 million. A player must match all 6 numbers to win the jackpot; players win prizes ranging from \$3 to \$100,000 for matching less than all 6 numbers. Drawings are held twice weekly on Wednesday and Saturday nights. For any drawing, if no ticket matches 6 out of 6 numbers, the jackpot rolls over to the next drawing to create a progressive jackpot. In March 2001, the Lottery added Power Play to the Powerball game. For an additional bet, the Power Play option provides non-jackpot winners the chance to multiply their prize amount by a factor of two through five.

The Montana Ca\$h game allows players the chance to win a minimum pari-mutuel jackpot of \$20,000. Players select 5 numbers from a field of 37 and must match at least 3 out of 5 to win a prize. Matching 3 of 5 wins \$5 and 4 of 5 wins \$200. The drawing is conducted twice weekly on Wednesday and Saturday nights. If no ticket matches all 5 numbers, the jackpot rolls over to the next drawing to create a progressive jackpot.

The Wild Card game allows players the chance to win a pari-mutuel jackpot, with a guaranteed minimum of \$100,000. Players select 5 numbers from a field of 31 plus one of 16 face cards and must match all 5 numbers and the wild card to win the jackpot; players win prizes from \$1 to \$5,000 for matching less than all 5 numbers and/or the wild card. Drawings are held twice weekly on Wednesday and Saturday nights. If no ticket matches all 5 numbers and the wild card, the jackpot rolls over to the next drawing to create a progressive jackpot.

The Lottery introduced Hot Lotto on April 7, 2002, replacing Rolldown. Hot Lotto allows players the chance to win a pari-mutuel jackpot with a guaranteed minimum of \$1 million. Players choose 5 numbers from a field of 39 plus 1 Hot Ball number from a field of 19; the first 5 numbers and the Hot Ball must be matched to win the jackpot. Players can win prizes ranging from \$2 to \$10,000 by matching less than all 5 numbers and/or the Hot Ball. If no ticket wins the jackpot, it rolls over to the next drawing to create a progressive jackpot. Drawings are held twice weekly on Wednesday and Saturday nights.

Rolldown provided a feature different from any other lotto game; for each drawing, if no ticket won the jackpot, all of the jackpot prize money was distributed to the three lower-tier prize levels on a pari-mutuel basis. Rolldown was discontinued on April 7, 2002.

9. COMMITMENTS - GAMING SUPPLIER CONTRACTS

Instant Tickets. On June 27, 2001 the Montana Lottery Commission approved the award of a one-year contract with Oberthur Gaming Technologies Corp. (Oberthur) for the provision of instant tickets; the resulting contract was signed on August 8, 2001. The contract is for one year with the option for six additional one-year renewals. The contract contains specifications regarding ticket design, printing, game ownership, inspection, and prize structure

Oberthur, as the vendor, provided a performance bond covering the contract term and an errors and omissions policy covering an ultimate net loss of \$7,500,000. The Lottery may terminate this contract by providing proper notification to Oberthur.

On-line Services. On August 18, 1998, the Lottery signed a seven-year contract with Autotote Lottery Corporation to provide an on-line gaming system and associated services beginning March 28, 1999. The contract provides for payments to be made for the purchase of an on-line gaming system including terminals and software. The Lottery paid Autotote Lottery Corporation \$5,025,311 for the system on April 26, 1999. Payment under the contract is also based on 8.35% of weekly Lottery sales.

10. CONTINGENT LIABILITIES - PRIZE ANNUITIES

During fiscal year 1989, the Montana Lottery awarded four Big Spin Jackpot prizes totaling \$5,000,000. The Lottery made the initial payments to the winners in the amount of \$253,088 and on September 26, 1988 the Montana Lottery awarded annuities in the amount of \$2,350,180 to Western National Life. Through these annuities, Western National Life makes the remaining payments to the Big Spin Jackpot winners. As of March 31, 2003 the contingent liability for future prize payments funded through the purchase of annuities was \$950,588.

11. LOTTO*AMERICA/POWERBALL/TRI-WEST JACKPOT PRIZES

Jackpot prizes awarded in the Lotto*America/POWERBALL and TRI-WEST LOTTO games are funded through the purchase of U.S. Treasury Zero-Coupon Bonds purchased in the name of the Montana Lottery by MUSL. MUSL will cash the bonds each year as they mature and will wire the funds to the Lottery for payment to winners on the Anniversary date of the win.

On January 13, 1990 the Montana Lottery awarded its first Lotto*America jackpot prize totaling \$1,740,000. The first annual payment of \$87,000 was made on February 1, 1990. On May 9, 1990 the Lottery awarded a second Lotto*America

jackpot prize of \$3,000,000. The first annual payment of \$150,000 was made on May 23, 1990. A third jackpot prize was awarded on February 2, 1991 for \$7,360,000. The first annual payment of \$368,000 was made February 15, 1991. On November 23, 1991 a fourth jackpot prize was awarded totaling \$46,967,738.57. The first annual payment of \$2,355,738.57 was made December 12, 1991. On April 11, 1992 a fifth jackpot prize was won totaling \$2,000,000. The first annual payment of \$100,000 was made on April 27, 1992.

On July 6, 1994 the Montana Lottery awarded its first Tri-West Lotto jackpot prize totaling \$700,565. The first annual payment of \$35,000 was made on July 26, 1994.

On July 22, 1995 the Montana Lottery awarded its first Powerball jackpot prize totaling \$31,401,655.99. The first payment of \$1,571,655.99 was made on August 8, 1995. On April 5, 1997 the Lottery awarded a second Powerball jackpot prize totaling \$11,000,000. The first annual payment of \$550,000 was awarded on April 18, 1997.

As of March 31, 2003 the combined total of future prize payments funded through the purchase of U.S. Treasury Zero-Coupon Bonds for Lotto*America winners was \$23,832,731. The combined total of future prize payments funded through the purchase of U.S. Treasury Zero-Coupon Bonds for Powerball and Tri-West Lotto winners was \$26,925,218.

On March 27, 1999 the Montana Lottery had a Powerball jackpot winner. The prize was \$35.1 million (\$19.35 million cash option). The winner chose the cash option and was paid a lump sum in June 1999.

12. LEASES

Rent. The Montana Lottery leases its office, administrative and warehouse facilities under a noncancelable lease agreement that is effective March 2002 through February 2007. The monthly lease payments through February 2004 are \$7,257 and will increase 1.5% per year.

13. LONG-TERM DEBT

Note Payable. A contract with Autotote Lottery Corporation required the purchase of an online gaming system including terminals and software. The Lottery paid Autotote Lottery Corporation \$5,025,311 for the system by entering into a loan agreement with Norwest Investment Service, now known as Wells Fargo Brokerage

Services, LLC. The loan will be repaid in quarterly installments of \$286,394.30 over five years. The first payment was due July 26, 1999. The interest rate on the loan is 5.12%.

Maturities of Long-term Debt

Year Ended June 30,

2003	1,054,786
2004	1,109,836
2005 and beyond	0
Total	<u>\$ 2,164,622</u>

14. CHANGE IN ACCOUNTING PRINCIPLE

Effective for the year beginning July 1, 2001, the Lottery adopted the provisions of Governmental Accounting Standards Board Statement No. 34, *Basic Financial Statements – and Management's Discussion and Analysis – for State and Local Governments*. The adoption resulted in a change in the format and content of the basic financial statements as follows: contributed capital is included as net assets and compensated absences is divided into current and long-term portions. The reported net assets that resulted from this change were included in the transfer to the State's General Fund for the quarter ending June 30, 2002.

Alternative accessible formats of this document will be provided upon request.